

Meeting of the

# AUDIT COMMITTEE

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Tuesday, 25 September 2012 at 7.00 p.m.

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## SUPPLEMENTARY AGENDA

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### VENUE

MEETING ROOM C1, FIRST FLOOR, TOWN HALL, MULBERRY  
PLACE, 5 CLOVE CRESCENT, LONDON, E14 2BG

Members:	Deputies (if any):
Chair: Councillor Carlo Gibbs Vice Chair: Councillor Anwar Khan <input type="checkbox"/>	
Councillor Craig Aston Councillor Stephanie Eaton Councillor Abdal Ullah Councillor David Edgar 1 Vacancy	Councillor David Snowdon, (Designated Deputy representing Councillor Craig Aston) Councillor Motin Uz-Zaman, (Designated Deputy representing Councillors Carlo Gibbs, David Edgar, Anwar Khan and Abdal Ullah) Councillor Marc Francis, (Designated Deputy representing Councillors Carlo Gibbs, David Edgar, Anwar Khan and Abdal Ullah,) Councillor Carli Harper-Penman, (Designated Deputy representing Councillors Carlo Gibbs, David Edgar, Anwar Khan and Abdal Ullah)

**[Note: The quorum for this body is 3 Members].**

If you require any further information relating to this meeting, would like to request a large print, Braille or audio version of this document, or would like to discuss access arrangements or any other special requirements, please contact: Antonella Burgio, Democratic Services  
Tel: 020 7364 4881, E-mail: [antonella.burgio@towerhamlets.gov.uk](mailto:antonella.burgio@towerhamlets.gov.uk)



**LONDON BOROUGH OF TOWER HAMLETS**

**AUDIT COMMITTEE**

**Tuesday, 25 September 2012**

**7.00 p.m.**

**5.1 Annual Governance Report - Council Accounts 2011-2012 (Pages 1 - 34)**

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# Annual governance report

London Borough of Tower Hamlets

Audit 2011/12

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Agenda Item 5.1



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# Key messages

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**This report summarises the findings from the 2011/12 audit which is substantially complete. It includes the messages arising from my audit of your financial statements and the results of the work I have undertaken to assess your arrangements to secure value for money in your use of resources.**

## **Financial statements**

As at 19 September I expect to issue an unqualified audit opinion by 28 September 2012. A number of errors were identified in the course of the audit. These concerned the disclosure of information in the notes to the financial statements and therefore did not impact on the Council's out-turn for the year or its available resources. My work also identified a number of uncertainties in the financial statements. We are satisfied that these do not have a material impact on the financial statements.

## **Value for money (VFM)**

I expect to conclude that you have made proper arrangements to secure economy, efficiency and effectiveness in your use of resources.

## **Certificate**

I plan to issue my certificate closing the audit by 5 October 2012.

# Before I give my opinion and conclusion

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**My report includes only matters of governance interest that have come to my attention in performing my audit. I have not designed my audit to identify all matters that might be relevant to you.**

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## **Independence**

I can confirm that I have complied with the Auditing Practices Board's ethical standards for auditors, including ES 1 (revised) – Integrity, Objectivity and Independence.

I am not aware of any relationships that may affect the independence and objectivity of the Audit Commission, the audit team or me, that I am required by auditing and ethical standards to report to you.

During the year the Audit Commission's Audit Practice undertook non-audit work for the Council for a fee of £4,500. The Audit Commission provided the Council with a tailored fraud briefing which will be presented to the September Audit Committee.

## **I ask the Audit Committee to:**

- consider the matters raised in this report before approving the financial statements;
- take note of the adjustments to the financial statements included in this report (appendices 2 and 3);
- approve the letter of representation (appendix 4), on behalf of the Council before I issue my opinion and conclusion; and
- agree your response to the proposed action plan (appendix 6).



# Financial statements

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**The Council's financial statements and annual governance statement are important means by which the Council accounts for its stewardship of public funds. As elected Members you have final responsibility for these statements. It is important that you consider my findings before you adopt the financial statements and the annual governance statement.**

## **Opinion on the financial statements**

Subject to satisfactory clearance of outstanding matters, I plan to issue an audit report, including an unqualified opinion on the financial statements, by 28 September 2012. Appendix 1 contains a copy of my draft audit report.

As at 19 September 2012, the main areas of outstanding work are:

- central government creditors;
- expenditure; and
- cash and bank.

## **Uncertainties in the financial statements**

My testing of sundry creditors, sundry debtors and income found:

- £7.008 million of sundry creditors could not be supported, largely because it related to historic items. In addition, an estimated £2.200 million of debtors were incorrectly netted off these creditors;
- schools debtors included in sundry debtors contained a balance of £7k that could not be fully agreed to supporting documentation. As a result debtors are potentially understated by an extrapolated total of £0.724 million;
- the Council Tax debtors included in sundry debtors could not be fully reconciled to the Council Tax system and may be understated by £0.329 million as a result;
- the HMRC creditor could not be fully reconciled to supporting documentation and could be overstated by £0.301 million; and
- a government grant creditor of £0.552 million could not be fully supported leading to a possible uncertainty of £0.857 million.

These matters are uncertainties so the financial statements have not been updated to correct them. I estimate that the maximum net impact of these uncertainties is that:

- creditors are overstated by £10.366 million;
- debtors are understated by £3.253 million;
- income is understated by £1.053 million;
- expenditure is overstated by £8.166 million; and
- the Council's surplus for the year is understated by £9.219 million.

### **Corrected errors**

In 2010/11 the Council omitted £116.873 million of grant income from the notes to the financial statements. This error was restricted to the notes and did not have an effect on the Council's Comprehensive Income and Expenditure Statement. The draft financial statements contained amended prior year comparators in note 37 but did not disclose that a prior period adjustment had been made. The financial statements have now been updated to include details of the prior period adjustment in Note 3.

The Council has an ongoing programme to improve the asset register by agreeing it to other sources of evidence. This work identified that the St Paul's Way School achieved Trust status in 2010/11 and that the school building, valued at £76.9 million, should have been removed from the Council's balance sheet. To correct this error, the Council treated this as a disposal in the 2011/12 financial statements.

### **Recommendations**

- R1** Account for prior year errors in accordance with International Accounting Standards. Where there is doubt as to whether a prior period adjustment should be made, the proposed treatment should be discussed with the audit team as early as possible.
- R2** Continue the programme of work to review the robustness of the data in the fixed asset register.

### **Significant risks and my findings**

I reported to you in my 20 March 2012 Audit Plan the significant risks that I identified relevant to my audit of your financial statements. Table 1 reports my findings against each of these risks.

Table 1: **Risks and findings**

Risk	Finding
<p><b>Heritage assets</b></p> <p>The 2011/12 IFRS Code adopts the requirements of FRS 30 Heritage Assets for the first time. These are assets held by the Council with the intention of preserving them for future generations because of their cultural, environmental or historical associations. Typical examples in local government include mayoral regalia and paintings. The standard requires that where information on cost or value is available, heritage assets must be reported on the Council's balance sheet and accounted for in accordance with the Code and its disclosure requirements. There is a risk that due to the difficulty in identifying and valuing heritage assets, this change in accounting policy may not be implemented correctly.</p>	<p>The Council undertook early work in this area to identify and value its heritage assets. This allowed early testing of this complex area. My work did not identify any errors in the Council's financial statements in relation to heritage assets.</p>
<p><b>ALMO pension liability</b></p> <p>The 2009/10 audit identified that the provision for the post-transfer service element of the ALMO pension liability was not accounted for in accordance with accounting standards. Whilst the error that has resulted in prior years from the Council's treatment of this item was not material, the value may increase as a result of changes in actuarial projections.</p>	<p>My testing of the accounting treatment of the post-transfer service element of the ALMO pension liability did not identify any material errors. This year's actuarial valuation resulted in the ALMO having a net asset in relation to pension costs. As a result, no provision is required in the Council's statements in relation to this item in 2011/12.</p>
<p><b>Housing Revenue Accounts (HRA) reform</b></p> <p>The government plans to reform local authority housing finance by adopting a self-financing model from 1 April 2012. For the Council this will be through a one-off settlement payment from central government on or before 28 March 2012. This will adjust the HRA debt of the Authority. Payments from government will in most cases be used to redeem an equal amount of all PWLB debt held by the Council. Due to the complexity, magnitude and timing of the HRA reform, there is risk that the financial statements may be materially misstated.</p>	<p>My testing did not identify any material errors in the accounting transactions relating to the HRA reform.</p>

## Risk

### Accruals

International Standards on Auditing (ISA 240 UK&I) presume an inherent risk in relation to revenue recognition for all audits. Given the pressures placed on council finances by the local government finance settlement, the risk of misstatement exceeds that of prior years particularly with regard to management accruals of expenditure.

## Finding

The Council was unable to support the split of accruals and creditors in note 22. The uncertainty was addressed by removing the distinction between accruals, initially reported as £8.833 million, and creditors in the note. Separate disclosure of accruals and creditors is not required by the Code but gives the reader of the accounts a better understanding of the Council's financial position. Whilst accruals are a form of creditors, they are accounting estimates and the value included in the statements is inherently less certain than other creditors.

The amendment did not have an impact on the Council's financial out-turn or available resources but does indicate a weakness in the processes to compile the financial statements.

The results of my testing of creditors has identified issues with accruals which are reported elsewhere in this report.

### Allocation of transactions to financial reporting periods

My grant certification work identified weaknesses in the Council's controls to ensure that transactions are allocated to the correct financial reporting period.

My testing of the allocation of transactions to financial reporting periods did not identify any errors that I need to bring to your attention.

## Recommendation

**R3** Undertake a review of the systems reports used to identify accruals and correctly identify accruals for separate reporting in the 2012/13 financial statements.

## Significant weaknesses in internal control

It is the responsibility of the Council to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. My responsibility as your auditor is to consider whether the Council has put adequate arrangements in place to satisfy itself that the systems of internal financial control are both adequate and effective in practice.

I have tested the Council's controls only to the extent necessary for me to complete my audit. I am not expressing an opinion on the overall effectiveness of internal control. I have reviewed the Annual Governance Statement and can confirm that:

- it complies with the requirements of CIPFA/SOLACE Delivering Good Governance in Local Government Framework; and
- it is consistent with other information that I am aware of from my audit of the financial statements.

### Control weaknesses

My testing of the Council's financial systems found a number of instances where the operation of controls was not evidenced. Examples included, but were not limited to:

- the weekly reconciliation of the Housing Rents and Service Charge systems to the general ledger; and
- the review of the monthly treasury reconciliation.

These weaknesses do not necessarily indicate control failures. They do, however, mean that I have been unable to place reliance on the Council's systems in these areas. As a result, I have undertaken additional substantive testing.

### Accounts payable control weaknesses

My testing of the accounts payable system identified a case where goods or services were recorded as having been received before the order had been completely fulfilled. This was possible because a single order was raised for numerous items and when one item was received the whole order was marked as complete. Whilst the total value of the order was £500, the error increases the risk that either creditors are raised or payments are made before goods or services are received. To address this risk I undertook additional substantive testing of transactions and balances derived from the accounts payable system.

My substantive testing of creditors and accruals identified a number of errors, including:

- historic balances which the Council was unable to support;
- debtors being inappropriately netted off against creditors; and
- accruals not adjusted to reflect the amount invoiced by the supplier.

Officers accept that there is much historic data held on the accounts payable system. The Council plans to introduce a new financial system from April 2012 and should use this opportunity to cleanse the data held on the accounts payable system before it is transferred to the new system. The impact of these errors is covered in the uncertainties section of this report on page 5.

## Recommendations

- R4** Evidence the operation of controls more consistently to strengthen the internal control environment.
- R5** Implement controls to prevent the pre-receipting of goods and services in the accounts payable system.
- R6** As part of the work to migrate the accounts payable data to the new system, undertake a thorough review of all creditor balances to ensure the data held is robust.

## Other matters

I am required to report significant findings from the audit and other matters that are significant to your oversight of the Council's financial reporting process including the following:

- Qualitative aspects of your accounting practices.
- Matters specifically required by other auditing standards to be communicated to those charged with governance. For example, issues about fraud, compliance with laws and regulations, external confirmations and related party transactions.
- Other audit matters of governance interest.

Table 2: Other matters

Issue	Finding
Related party transactions – note 38	I evaluated the Council's arrangements for identifying and disclosing related parties within its financial statements. I reviewed the disclosure in note 38 and found that it disclosed bodies that do not meet the definition of a related party as prescribed by IAS 24. The note has been updated to correct this and to provide the reader with clearer information about the Council's related party transactions.
Cash reconciliations	I tested a sample of cash account reconciliations. I found that there was an unreconciled difference of £793 on a closed bank account. Whilst the amount is small, this indicates weaknesses in the Council's cash management arrangements.

Issue	Finding
<p>Audit fee</p>	<p>The audit fee disclosed in note 35 incorrectly included a fee of £32k for the Pension Fund and the fees for other services payable by external auditors was overstated by £5k. The financial statements have been updated to correct these errors. It is important that the audit fee is reported accurately in the financial statements because it gives the reader of the accounts information which may affect their view of my independence.</p>
<p>Foreword to the financial statements</p>	<p>I review the information included in the foreword to the financial statements to ensure that it is consistent with my knowledge. This work found that there were errors in the financial information included in the foreword. For example:</p> <ul style="list-style-type: none"> <li>■ gross expenditure was overstated by £3.2 million in the foreword; and</li> <li>■ revenue funding sources were overstated by £13.37 million in the foreword.</li> </ul> <p>The foreword has been updated to correct these errors.</p>
<p>Prior year comparators</p>	<p>My agreement of the prior year comparators the to 2010/11 audited financial statements found that the comparators had been changed in the following notes without a disclosed prior period adjustment:</p> <ul style="list-style-type: none"> <li>■ Note 29 – Trading operations;</li> <li>■ Note 33 – Remuneration; and</li> <li>■ Note 39 – Leases.</li> </ul> <p>None of the changes were significant and therefore prior period adjustments were not required. The notes have been updated to show the audited prior year comparators.</p>

**Recommendation**

- R7** Undertake a thorough review of the financial statements and supporting working papers prior to submission for audit. In particular, consider whether:
- the related party transactions note is clear and in accordance with IAS 24;
  - all cash reconciliations have been completed without un-reconciled items;
  - the foreword to the financial statements agrees to those statements; and
  - the audit fee is accurately disclosed.

## **Whole of Government Accounts**

Alongside my work on the financial statements, I also review and report to the National Audit Office on your Whole of Government Accounts return. The Council submitted its draft return to the Department for Communities and Local Government on 8 August 2012 which was after the statutory deadline of 27 July 2012. Subject to the resolution of outstanding testing of sundry debtors and creditors I expect to complete my report by the deadline of 5 October.



# Value for money

**I am required to conclude whether the Council put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. This is the value for money conclusion.**

I assess your arrangements against the two criteria specified by the Commission. In my 20 March 2012 Audit Plan I reported to you the significant risks that were relevant to my conclusion. I have set out below my conclusion on the two criteria, including the findings of my work addressing each of the risks I identified.

I intend to issue an unqualified conclusion stating that the Council has proper arrangements to secure economy, efficiency and effectiveness in the use of its resources. I include my draft conclusion in appendix 1.

Table 3: Value for money conclusion criteria and my findings

Criteria	Findings
<p><b>1. Financial resilience</b></p> <p>The organisation has proper arrangements in place to secure financial resilience.</p> <p>Focus for 2011/12:</p> <p>The organisation has robust systems and processes to manage effectively financial risks and opportunities, and to secure a stable financial position that enables it to continue to operate for the foreseeable future.</p> <p>Risk reported in my audit plan:</p> <p>The Council has made significant changes to its medium term financial plan in response to the recession, Comprehensive Spending Review (CSR) and the resulting increased financial pressures.</p>	<p>My review of the Council's arrangement to achieve financial resilience found that the Council has adequate arrangements in place.</p> <p>The Council set and achieved a balanced budget in 2011/12 and has a balanced budget for 2012/13. Whilst the Council's financial planning arrangements are sound, significant further financial pressures are forecast in the short to medium term. The Council should continue to review and update its financial plans in response to changes in funding and demand for services.</p> <p>My testing of accounts payable and receivable identified weaknesses in the data held on the Council's financial systems. Elsewhere in my report I have recommended that management take action to correct these issues.</p>

Criteria	Findings
<p><b>2. Securing economy efficiency and effectiveness</b></p> <p>The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.</p> <p>Focus for 2011/12:</p> <p>The organisation is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.</p> <p>Risk reported in my audit plan:</p> <p>The Council's move to a mayoral system has resulted in changes to the Council's governance arrangements.</p>	<p>My review of the Council's arrangements to secure economy, efficiency and effectiveness in its use of resources found that that its arrangements are sound.</p> <p>Changes were made to the Council's governance arrangements in 2010/11 in response to the move to a Mayoral system. These arrangements have now been embedded but by its nature, this is an area that is subject to ongoing change. The Council should maintain a watching brief on the adequacy of its governance arrangements.</p>

**Recommendations**

- R8** Continue to review and update the Council's financial plans in response to changes in funding and demand for services.
- R9** Maintain a watching brief on the adequacy of the Council's governance arrangements.

# Fees

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## I reported my planned audit fee in the 20 March 2012 Audit Plan.

I expect to complete the audit within the planned fee.

Table 4: Fees

	Planned fee 2011/12 (£)	Expected fee 2011/12 (£)
Audit	462,150	462,150
Claims and returns	96,000	96,000
Non-audit work	4,500	4,500
<b>Total</b>	<b>562,650</b>	<b>562,650</b>

# Appendix 1 – Draft independent auditor’s report

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## INDEPENDENT AUDITOR’S REPORT TO THE MEMBERS OF THE LONDON BOROUGH OF TOWER HAMLETS

### Opinion on the financial statements

I have audited the financial statements of the London Borough of Tower Hamlets for the year ended 31 March 2012 under the Audit Commission Act 1998. The financial statements comprise the Authority and Group Movement in Reserves Statement, the Authority and Group Comprehensive Income and Expenditure Statement, the Authority and Group Balance Sheet, the Authority and Group Cash Flow, the Housing Revenue Account Income and Expenditure Statement, the Movement on the Housing Revenue Account Statement, the Collection Fund and the related notes. The financial reporting framework applied to their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2011/12.

This report is made solely to the members of the London Borough of Tower Hamlets in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and Audited Bodies published by the Audit Commission in March 2010.

### Respective responsibilities of the Corporate Director of Resources and the auditor

As explained more fully in the Statement of the Corporate Director of Resources’ Responsibilities, the Corporate Director of Resources is responsible for the preparation of the Statement of Accounts, which includes the financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom, and for being satisfied that they give a true and fair view. My responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require me to comply with the Auditing Practices Board’s Ethical Standards for Auditors.

### Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Authority and Group’s circumstances and have been consistently applied and adequately disclosed; the

reasonableness of significant accounting estimates made by the Corporate Director of Resources; and the overall presentation of the financial statements. In addition, I read all the financial and non-financial information in the explanatory foreword to identify material inconsistencies with the audited financial statements. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

### **Opinion on financial statements**

In my opinion the financial statements:

- give a true and fair view of the financial position of the London Borough of Tower Hamlets as at 31 March 2012 and of its expenditure and income for the year then ended;
- give a true and fair view of the financial position of the Group as at 31 March 2012 and of its expenditure and income for the year then ended; and
- have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2011/12.

### **Opinion on other matters**

In my opinion, the information given in the explanatory foreword for the financial year for which the financial statements are prepared is consistent with the financial statements.

### **Matters on which I report by exception**

I report to you if:

- in my opinion the annual governance statement does not reflect compliance with 'Delivering Good Governance in Local Government: a Framework' published by CIPFA/SOLACE in June 2007;
- I issue a report in the public interest under section 8 of the Audit Commission Act 1998;
- I designate under section 11 of the Audit Commission Act 1998 any recommendation as one that requires the Authority to consider it at a public meeting and to decide what action to take in response; or
- I exercise any other special powers of the auditor under the Audit Commission Act 1998.

I have nothing to report in these respects.

### **Opinion on the pension fund financial statements**

I have audited the pension fund financial statements for the year ended 31 March 2012 under the Audit Commission Act 1998. The pension fund financial statements comprise the Fund Account, the Net Assets Statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2011/12.

This report is made solely to the members of the London Borough of Tower Hamlets in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and Audited Bodies published by the Audit Commission in March 2010.

### **Respective responsibilities of the Corporate Director of Resources and auditor**

As explained more fully in the Statement of the Corporate Director of Resources' Responsibilities, the Corporate Director of resources is responsible for the preparation of the Authority and Group's Statement of Accounts, which includes the pension fund's financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom, and for being satisfied that they give a true and fair view. My responsibility is to audit and express an opinion on the accounting statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require me to comply with the Auditing Practices Board's Ethical Standards for Auditors.

### **Scope of the audit of the financial statements**

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Corporate Director of Resources; and the overall presentation of the financial statements. In addition, I read all the financial and non-financial information in the explanatory foreword to identify material inconsistencies with the audited financial statements. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

### **Opinion on financial statements**

In my opinion the pension fund's financial statements:

- give a true and fair view of the financial transactions of the pension fund during the year ended 31 March 2012 and the amount and disposition of the fund's assets and liabilities as at 31 March 2012; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2011/12.

### **Opinion on other matters**

In my opinion, the information given in the explanatory foreword for the financial year for which the financial statements are prepared is consistent with the financial statements.

## **Conclusion on Authority's arrangements for securing economy, efficiency and effectiveness in the use of resources**

### **Respective responsibilities of the Authority and the auditor**

The Authority is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to review regularly the adequacy and effectiveness of these arrangements.

I am required under Section 5 of the Audit Commission Act 1998 to satisfy myself that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the Audit Commission requires me to report to you my conclusion relating to proper arrangements, having regard to relevant criteria specified by the Audit Commission.

I report if significant matters have come to my attention which prevent me from concluding that the Authority has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. I am not required to consider, nor have I considered, whether all aspects of the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

### **Scope of the review of arrangements for securing economy, efficiency and effectiveness in the use of resources**

I have undertaken my audit in accordance with the Code of Audit Practice, having regard to the guidance on the specified criteria, published by the Audit Commission in October 2011, as to whether the Authority has proper arrangements for:

- securing financial resilience; and
- challenging how it secures economy, efficiency and effectiveness.

The Audit Commission has determined these two criteria as those necessary for me to consider under the Code of Audit Practice in satisfying myself whether the Authority put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2012.

I planned my work in accordance with the Code of Audit Practice. Based on my risk assessment, I undertook such work as I considered necessary to form a view on whether, in all significant respects, the Authority had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

### **Conclusion**

On the basis of my work, having regard to the guidance on the specified criteria published by the Audit Commission in October 2011, I am satisfied that, in all significant respects, the London Borough of Tower Hamlets put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2012.

### **Delay in certification of completion of the audit**

I cannot formally conclude the audit and issue an audit certificate as I am still to complete the work necessary to issue my assurance statement in respect of the Council's Whole of Government Accounts consolidation pack. I am satisfied that this work does not have a material effect on the financial statements or on my value for money conclusion.

Jon Hayes

District Auditor

1<sup>st</sup> Floor Millbank Tower, Millbank, London, SW1P 4HQ

xx September 2012



# Appendix 2 – Corrected errors

I identified the following errors during the audit which management have addressed in the revised financial statements.

Nature of error	Item of account	Statement of comprehensive income and expenditure		Balance sheet	
		Dr £'000s	Cr £'000s	Dr £'000s	Cr £'000s
<b>Note 22 (creditors)</b>					
Accruals disclosed in the financial statements could not be reliably distinguished from creditors	Accruals			8,833	
The NDR creditor was not fully aggregated into a single balance in the financial statements	Creditors				8,833
	Debtors – other entities and individuals	355			
	Creditors – central government bodies		3,770		
	Creditors – other entities and individuals	3,415			
<b>Collection Fund</b>					
The transactions relating to the Business Rate Supplement (BRS) were not disclosed separately from National Non-Domestic Rates (NDR) transactions in the Collection Fund.	NDR income	12,006			
	BRS income		12,006		
	Cost of collection allowance		946		
	BRS cost of collection allowance	946			
	NDR payment to the national pool		11,973		
	BRS payment to the GLA	11,973			

## Other adjustments to the financial statements

Adjusted statement	Nature of adjustment
Statement of movement on reserves	The transfers in and out of the Improvement and Efficiency earmarked reserve were both overstated by £2,167k. These errors have been corrected and there was no net impact on reserves.
Note 35 (Audit fees)	<p>The following adjustments were made to correct overstatements in Note 35.</p> <ul style="list-style-type: none"> <li>■ Fees payable for audit services was reduced by £32k.</li> <li>■ Fees payable for non-audit services was reduced by £5k.</li> </ul> <p>The error was restricted to the note and there was no impact on the Comprehensive Income and Expenditure Account.</p>
Note 15 (Financial Instruments)	The financial instruments note has been updated to include a disclosure reflecting that the Council has issued financial guarantees to its ALMO and housing associations. Due to the nature of the guarantees, a value cannot be attributed to the guarantees.

# Appendix 3 – Draft letter of management representation

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## London Borough of Tower Hamlets – Audit for the year ended 31 March 2012

I confirm to the best of my knowledge and belief, having made appropriate enquiries of other [insert relevant details directors of the London Borough of Tower Hamlets, the following representations given to you in connection with your audit of the Council's financial statements for the year ended 31 March 2012.

### Compliance with the statutory authorities

I have fulfilled my responsibility under the relevant statutory authorities for preparing the financial statements in accordance with the Accounts and Audit (England) Regulations 2011 and the Code of Practice on Local Authority Accounting in the United Kingdom which give a true and fair view of the financial position and financial performance of the Council, for the completeness of the information provided to you, and for making accurate representations to you.

### Supporting records

I have made available all relevant information and access to persons within the Council for the purpose of your audit. I have properly reflected and recorded in the financial statements all the transactions undertaken by the Council.

### Irregularities

I acknowledge my responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud or error.

I also confirm that I have disclosed:

- my knowledge of fraud, or suspected fraud, involving either management, employees who have significant roles in internal control or others where fraud could have a material effect on the financial statements;
- my knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others; and
- the results of our assessment of the risk the financial statements may be materially misstated as a result of fraud.

### **Law, regulations, contractual arrangements and codes of practice**

I have disclosed to you all known instances of non-compliance, or suspected non-compliance with laws, regulations and codes of practice, whose effects should be considered when preparing financial statements.

Transactions and events have been carried out in accordance with law, regulation or other authority. The Council has complied with all aspects of contractual arrangements that could have a material effect on the financial statements in the event of non-compliance.

All known actual or possible litigation and claims, whose effects should be considered when preparing the financial statements, have been disclosed to the auditor and accounted for and disclosed in accordance with the applicable financial reporting framework.

### **Accounting estimates including fair values**

I confirm the reasonableness of the significant assumptions used in making the accounting estimates, including those measured at fair value.

### **Related party transactions**

I confirm that I have disclosed the identity of the Council's related parties and all the related party relationships and transactions of which I am aware. I have appropriately accounted for and disclosed such relationships and transactions in accordance with the requirements of the Code.

### **Subsequent events**

I have adjusted for or disclosed in the financial statements all relevant events subsequent to the date of the financial statements.

Signed on behalf of the London Borough of Tower Hamlets

I confirm that the this letter has been discussed and agreed by the Audit Committee on 25 September 2012

Signed

Name

Position

Date

# Appendix 4 – Glossary

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## **Annual Audit Letter**

Letter issued by the auditor to the Council after the completion of the audit that summarises the audit work carried out in the period and significant issues arising from the auditors' work.

## **Annual Governance Report**

The auditor's report on matters arising from the audit of the financial statements presented to those charged with governance before the auditor issues the opinion and conclusion.

## **Annual Governance Statement**

The annual report on the Council's systems of internal control that supports the achievement of the Council's policies aims and objectives.

## **Audit of the accounts**

The audit of the accounts of an audited body comprises all work carried out under the Code to meet the auditor's statutory responsibilities under the Audit Commission Act 1998.

## **Audited body**

A body to which the Audit Commission is responsible for appointing the external auditor.

## **Auditing Practices Board (APB)**

The body responsible in the UK for issuing auditing standards, ethical standards and associated guidance to auditors. Its objectives are to establish high standards of auditing that meet the developing needs of users of financial information and to ensure public confidence in the auditing process.

### **Auditing standards**

Pronouncements of the APB that contain basic principles and essential procedures with which auditors must comply, except where otherwise stated in the auditing standard concerned.

### **Auditor(s)**

Auditors appointed by the Audit Commission.

### **Code (the)**

The Code of Audit Practice for local government bodies issued by the Audit Commission and approved by Parliament.

### **Commission (the)**

The Audit Commission for Local Authorities and the National Health Service in England.

### **Ethical Standards**

Pronouncements of the APB that contain basic principles relating to independence, integrity and objectivity that apply to the conduct of audits and with which auditors must comply, except where otherwise stated in the standard concerned.

### **Financial statements**

The annual statement of accounts that the Council is required to prepare, which report the financial performance and financial position of the Council in accordance with the Accounts and Audit (England) Regulations 2011 and the Code of Practice on Local Authority Accounting in the United Kingdom.

### **Group accounts**

Consolidated financial statements of the Council and its subsidiaries, associates and jointly controlled entities.

### **Internal control**

The whole system of controls, financial and otherwise, that the Council establishes to provide reasonable assurance of effective and efficient operations, internal financial control and compliance with laws and regulations.

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### **Audit Commission**

## **Materiality**

The APB defines this concept as ‘an expression of the relative significance or importance of a particular matter in the context of the financial statements as a whole. A matter is material if its omission would reasonably influence the decisions of an addressee of the auditor’s report; likewise a misstatement is material if it would have a similar influence. Materiality may also be considered in the context of any individual primary statement within the financial statements or of individual items included in them. Materiality is not capable of general mathematical definition, as it has both qualitative and quantitative aspects’.

The term ‘materiality’ applies only to the financial statements. Auditors appointed by the Commission have responsibilities and duties under statute, as well as their responsibility to give an opinion on the financial statements, which do not necessarily affect their opinion on the financial statements.

## **Significance**

The concept of ‘significance’ applies to these wider responsibilities and auditors adopt a level of significance that may differ from the materiality level applied to their audit of the financial statements. Significance has both qualitative and quantitative aspects.

## **Those charged with governance**

Those entrusted with the supervision, control and direction of the Council. This term includes the members of the Council and its Audit Committee.

## **Whole of Government Accounts**

A project leading to a set of consolidated accounts for the entire UK public sector on commercial accounting principles. The Council must submit a consolidation pack to the department for Communities and Local Government which is based on, but separate from, its financial statements.

# Appendix 5 – Action plan

## Recommendations

### Recommendation 1

Account for prior year errors in accordance with International Accounting Standards. Where there is doubt as to whether a prior period adjustment should be made, the proposed treatment should be discussed with the audit team as early as possible.

**Responsibility** Kevin Miles

**Priority** Medium

**Date** March 2013

**Comments** Officers will liaise with auditors during year if potential PPAs are identified to agree how they should be treated.

### Recommendation 2

Continue the programme of work to review the robustness of the data in the fixed asset register.

**Responsibility** Kevin Miles

**Priority** Medium

**Date** March 2013

**Comments** Officers will continue to liaise with property and legal services in reconciling the accounting fixed asset register to Council records. Officers will liaise with CSF officers to highlight where the status of a school or building may change in future.



## Recommendations

### Recommendation 3

Undertake a review of the systems reports used to identify accruals and correctly identify accruals for separate reporting in the 2012/13 financial statements.

<b>Responsibility</b>	Kevin Miles
<b>Priority</b>	Medium
<b>Date</b>	March 2013
<b>Comments</b>	Officers will clarify the approach for identifying accruals with the auditors. Annual closedown guidance to budget managers will be updated to ensure accruals are identified.

### Recommendation 4

Evidence the operation of controls more consistently to strengthen the internal control environment.

<b>Responsibility</b>	Alan Finch, Paul Thorogood & Minesh Jani
<b>Priority</b>	High
<b>Date</b>	December 2012
<b>Comments</b>	Officers will review processes for the reconciliation of rent and service charge systems and treasury to ensure undertaken. Reconciliations will be incorporated into the new financial system during the implementation process. Internal Audit will carry out a review to provide assurance that reconciliations have been carried out for the first six months of 2012/13 and evidenced.

## Recommendations

### Recommendation 5

Implement controls to prevent the pre-receipting of goods and services in the accounts payable system.

<b>Responsibility</b>	Minesh Jani & Paul Thorogood
<b>Priority</b>	High
<b>Date</b>	December 2012
<b>Comments</b>	Officers will conduct a review during the year to ensure material pre-receipting has not been performed on R2P. New system guidance will remind officers that pre-receipting (where payment in advance is not required) is contrary to financial regulations.

### Recommendation 6

As part of the work to migrate the accounts payable data to the new system, undertake a thorough review of all creditor balances to ensure the data held is robust.

<b>Responsibility</b>	Kevin Miles
<b>Priority</b>	High
<b>Date</b>	March 2013
<b>Comments</b>	Debtor and creditor balances will be reviewed as part of the data migration to the new finance system.

## Recommendations

### Recommendation 7

Undertake a thorough review of the financial statements and supporting working papers prior to submission for audit. In particular, consider whether:

- the related party transactions note is clear and in accordance with IAS 24;
- all cash reconciliations have been completed without un-reconciled items;
- the foreword to the financial statements agrees to those statements; and
- the audit fee is accurately disclosed.

**Responsibility** Kevin Miles

**Priority** Medium

**Date** June 2013

**Comments** Officers will conduct a thorough review of the accounts as possible, before publication of the draft accounts and prior to the start of the audit.

### Recommendation 8

Continue to review and update the Council's financial plans in response to changes in funding and demand for services.

**Responsibility** Alan Finch

**Priority** High

**Date** Ongoing

**Comments** As part of the budget process, officers will continue to monitor Government announcements and pressures on services to ensure risk is adequately understood and referenced to plans.

## Recommendations

### Recommendation 9

Maintain a watching brief on the adequacy of the Council's governance arrangements.

<b>Responsibility</b>	Chris Naylor & Isabella Freeman
<b>Priority</b>	High
<b>Date</b>	Ongoing
<b>Comments</b>	The CFO and Monitoring Officer will maintain an oversight of governance arrangements through appropriate use of internal controls.

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